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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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Federal Communications Commission
Office of Secretary

In the Matter of	)	
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Implementation of the Pay Telephone	)	
Reclassification and Compensation	)	CC Docket No. 96-128
Provisions of the Telecommunications	)	
Act of 1996	)	

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PETITION OF SPRINT FOR RECONSIDERATION

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October 21, 1996

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SUMMARY

The Commission's payphone compensation program is misconceived in every important respect. Sprint urges the Commission to rescind its Report and Order in toto.

The Commission has created a $1 billion annual corporate welfare program for PSPs without any showing of need by the payphone industry, without any regard to the evidence of record as to payphone costs and revenue streams, and without any consideration of the impact this program will have on IXCs, and ultimately, consumers.

The first-year recovery mechanism is arbitrary because of the lack of any demonstrated relationship between overall toll revenues and the types of calls that are compensable. By excluding smaller IXCs and all LECs, it also discriminates against larger IXCs, inflating their payments by 25%. Basing the compensation level on deregulated local coin rates after the second year creates administrative problems for the IXCs and an enormous opportunity for fraud by PSPs, and gives PSPs an incentive to increase their rates to the public.

The Commission erred in including international calls as compensable. There is no statutory basis for doing so, and the Commission provided no reasoned explanation of why it believed it had the authority to do so.

The Commission should have opted for the "set use fee" approach to compensation, rather than "carrier-pays." The set

use fee will result in lower charges to consumers and will give visibility to the "tax" being imposed on them.

The Order also unfairly burdens "facilities-based carriers" with the obligation to compensate PSPs on behalf of resellers, with no assurance that the facilities-based carriers can in fact pass on these amounts to their reseller customers. Furthermore, the facilities-based carriers would be caught in the middle of disputes between PSPs and resellers over the amounts that are properly payable on the resellers' behalf. Instead, each carrier should be responsible for tracking and compensating PSPs for its own compensable calls.

Although the order requires that each payphone should be required to generate 07 or 27 coding digits within the ANI, the rules fail to reflect this requirement and should be amended accordingly.

Since emergency calls are not subject to per-call compensation, the LECs should provide, free of charge, a comprehensive list of emergency numbers to the IXCs.

The Commission must also clarify that the LECs should remove all payphone-related costs, not just the cost of the payphone itself, from the carrier common line charge.

Finally, the Commission should clarify that LECs need not provide installation and maintenance of payphone equipment as a service to competing PSPs.

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PETITION OF SPRINT FOR RECONSIDERATION

Sprint Corporation hereby seeks reconsideration of the September 20, 1996 Report and Order (FCC 96-388) in the above-captioned docket. In that order, the Commission created a $1 billion annual welfare program for payphone service providers (PSPs), at the expense of IXCs and their customers, without any showing of need by the PSPs. In so doing, the Commission has saddled IXCs with a substantial administrative burden and has created rife opportunities for fraud on the part of the payphone industry -- an industry that has helped to bring unconscionably high rates to the public for 0+ calls and has prompted tens of thousands of consumer complaints to the Commission.

The Commission's payphone compensation plan is so ill-conceived that, particularly in view of the tight statutory deadline for acting on this and other petitions for reconsideration, the best course of action would be for the Commission to rescind its order in toto. In the alternative, it should set the compensation rate at $0 per call unless or until the Commission has convincing evidence that any greater rate of compensation is indeed "fair."

I. THE BASIS FOR THE PER-CALL RATES ADOPTED BY THE COMMISSION IS WITHOUT FOUNDATION (¶¶67-76)

In setting the compensation rate at $.35 per call (or its per-line equivalent) for the first two years, and whatever charges are assessed thereafter for local coin calls, the Commission committed several fundamental errors.

1. The Commission ignored record evidence, submitted by the future recipients of this compensation, that the revenue streams already available to PSPs through 0+ commissions and local coin calls -- $3447 per phone per year -- is roughly double the RBOCs' estimate of the total annual costs of providing a payphone -- $1744. See Reply Comments of Sprint (at 16-17) and MCI (at 3).[1] Furthermore, the Commission ignored AT&T's evidence that its total cost of providing payphones is $885 per year -- only one-half the amount estimated by the RBOCs. See AT&T Reply Comments at 8-9. Given these facts, any per-call compensation for other call types -- dial-around operator services, prepaid card, and subscriber 800 -- is simply a windfall that, at least in the short run, unjustly enriches the PSPs at the expense of the

[1] The RBOC cost estimate included premises owner commissions. See RBOC Payphone Coalition Comments, Attach. at 9.

public that must ultimately pay for this corporate welfare program. Moreover, if competition in the payphone market is effective, even the intended recipients of this welfare program ultimately will not keep the lion's share of the windfall provided them. Rather, it will be "competed away" in the form of higher commission payments to premises owners who possess local market power over the siting of payphones.

2. There is nothing either in the record or in logic to support the notion that local coin rates are an appropriate measure of the costs of making payphone available for any other type of call.[2] When a payphone provider makes its phone available for toll calls, it is the IXCs who bear the costs of getting the call from the payphone premises to its intended destination: they pay the access charges on the local lines and switches involved, and pay for the long distance transmission to the destination of a call. By contrast, the local coin rate covers not only the cost of the equipment, but also the cost of the local line, local switching and transmission to the called party, plus the labor costs associated with periodic emptying of the coin box. The Commission itself, in 1991, estimated that the fully allocated cost of providing pay telephones exclusive of transmission and coin collection costs amounts to only $.12 per call,[3] only

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[2] See Sprint's Comments at 9, 21 and AT&T's Reply Comments at 11-14.

[3] See Operator Service Access 6 FCC Rcd 4736, 4747 (1991).

one-third the per-call compensation ordered herein. The Commission walked away from that analysis without ever explaining why it did so. See Report and Order, ¶68.

3. In addition to the fact, discussed above, that the regulated local coin rate is not an appropriate measure of the cost of making a phone available for an otherwise non-revenue-producing call, there is no basis for the Commission's belief that unregulated local coin rates have anything whatsoever to do with such costs. Although the Commission correctly observes in ¶70 that there are low entry and exit barriers in the payphone business, the Commission overlooks the fact that PSPs compete for locations based on the level of commissions they pay to the premises owners. This carries a built-in incentive to charge consumers as much as possible, in order to increase the commissions that can be offered to premises owners.

4. Even the fully allocated cost of providing payphones, as estimated by the Commission in 1991, is still far too high to ensure "fair" compensation. Given the freedom of entry into and exit from the payphone market, it can be presumed that the payphone providers place payphones in service only when they anticipate that the revenue streams available to them, from local coin rates, 0+ commissions or acting as the operator service provider, fully compensate them for the costs of the payphone. In these circumstances, the

appropriate measure of costs for other non-revenue-producing calls -- such as dial-around, subscriber 800, and prepaid card calls -- is the marginal cost of handling these additional calls. Indeed, twice in the NPRM (nn. 54 and 64) the Commission pointed to marginal costs as the relevant standard. The marginal costs of handling these additional calls amounts to nothing more than the wear and tear on the keypad and handset, and perhaps some unascertained opportunity costs.[4]

In ¶68 of the Report and Order, the Commission rejected both marginal cost pricing and incremental cost standards on the grounds that they "could leave PSPs without fair compensation for certain types of payphone calls, because such a standard would not permit the PSP to recover a reasonable share of the joint and common costs associated with those calls." (Footnote omitted.) This reasoning is a tautology: it assumes that "fair" compensation for these calls includes a share of joint and common costs. This assumption ignores the fact, shown by the PSPs' data (<u>see</u> p. 2, above), that the joint and common costs are more than fully recovered from other revenue streams. Nothing in the legislative history of §276 suggests that Congress intended the FCC to give a billion dollar windfall to payphone providers, or that it intended to attribute to the term "fair" anything other than the common

[4] For discussion of those opportunity costs, see Sprint's Comments, n.11 at 18, and Reply Comments, n.6 at 8-9.

sense meaning of "just" "reasonable" "passable" and "sufficient".[5] Certainly there is no reason to assume that Congress believed overrecovery of costs would be "fair." Under these circumstances, unless and until the payphone industry convincingly demonstrates, with comprehensive data, that it is incurring costs in handling non-revenue-producing calls, and that these costs are not covered by other revenue streams from payphone operations, the Commission should either decline to order any per-call compensation at all or set the rate at zero.

The Commission's order totally disregards the consequences of its corporate welfare program on those who must foot the bill. The $.35 per call charge exceeds, by a considerable margin, Sprint's gross revenues from a typical toll free call. Toll free subscribers who, by the nature of their business, receive a substantial number of calls from payphones (e.g., paging companies, trucking companies, and companies in travel related industries) will see a substantial increase in their costs for toll-free service, if IXCs decide to pass these charges through to the party paying for the underlying call. If, in the alternative, IXCs simply raise their overall rates for toll-free service to cover these increased costs, then all toll free customers will see their rates rise in order to compensate the PSPs.

[5] See Sprint's Reply Comments at 11.

There will also be a significant impact on persons using proprietary calling cards -- those for which a dial-around access code must be used. Many consumers were driven to use such calling cards because of the high rates PSPs and their chosen OSPs charged for 0+ calls from payphones. In recent months, there has been a trend in the direction of flat-rated charges for these calling card cards as an alternative to a high up-front surcharge. For example, Sprint recently introduced a calling card that has a flat rate of $.25 per minute, with no additional calling card surcharge. It is not clear whether this and similar offerings of competitors can be sustained when the IXCs are faced with such a high per-call rate. For example, the typical billable length of a Sprint calling card call is eight minutes, resulting in a revenue per call of $2.00. A $.35 charge imposed on Sprint represents 17.5% of the revenues from a typical card call.

Retail rates for prepaid calling cards have trended downward in the past few years and are presently in the neighborhood of $.30 per minute. Calls on prepaid cards tend to have a shorter duration than calling card calls -- the typical billable time is four minutes. A $.35 per call charge represents 29% of the amount paid by a consumer for a typical call. Clearly in that highly competitive segment of the market, there is no reason to believe that carriers can absorb a cost increase of this magnitude without raising their rates to consumers. Furthermore, the windfall gain to the PSPs will be accompanied, for a year or more, by an unrecoverable loss to prepaid card carriers. Prepaid cards typically have an expiration date of 15 months to two years and there are literally millions of cards outstanding with no expectation from the public that the charges for calls with these cards could rise before they expire. Thus, in the case of calling cards issued by IXCs who are liable to pay the per-call compensation to the PSPs, the IXCs have little choice but to absorb this additional expense with respect to outstanding cards and cards issued for sometime into the future.[6]

In short, the Commission's billion dollar corporate welfare program cannot be provided gratis. The piper must be paid, and paying the piper will have a substantial impact on IXCs and, ultimately, will result in significant increases in the rates end users must pay. Such an outcome, in the absence of any comprehensive showing of need by PSPs, can hardly be considered "fair."

II. THE FIRST-YEAR RECOVERY METHOD IS ARBITRARY AND DISCRIMINATES AGAINST LARGER IXCS (¶¶124-125)

During the first year of the payphone welfare program, private payphone providers are entitled to receive $45.85 per

[6] Sprint estimates it will take a year before its prepaid card platform can identify, on a real-time basis, that a call is coming from a payphone, and deduct a higher amount from the value of that card.

phone per month, rather than per-call compensation. This sum was obtained by multiplying a rate of $.35 per call times an assumed average of 131 access code calls and subscriber 800 calls per month. See ¶¶124-125. However, this amount is only to be recovered from IXCs with annual toll revenues in excess of $100 million, apportioned on the basis of their respective annual toll revenues. This apportionment of the first-year obligation is flawed in two respects.

First, there is no demonstrated relationship between an IXC's overall toll revenues and the particular types of calls found to be compensable. An IXC that concentrates its marketing efforts on compensable types of calls (such as MCI, with its heavy advertising of 1-800-COLLECT), may have a larger market share of compensable calls than its share of overall toll revenues, and thus will be paying less than its should in the first year. Other carriers that concentrate, for example, on 1+ traffic from businesses and households, may receive few compensable calls and will have to pay far in excess of their market share of such calls.

Second, the first year apportionment discriminates against larger IXCs. Both IXCs with toll revenues of less than $100 million per year and local exchange carriers of all sizes are freed of any compensation obligations during that period even though such carriers handle both intraLATA and interLATA calls from private payphones.[7] The Commission fails to offer a reasoned basis for excluding these other carriers from shouldering their fair share of the payment obligation. According to the Commission's most recent market share data, IXCs with less than $100 million in annual revenues account for nearly $5.2 billion in toll revenues, and the local exchange carriers account for $11.3 billion of toll revenues. Together, these groups comprise 20 percent of total toll revenues. See Common Carrier Bureau, "Long Distance Market Shares, Second Quarter 1996" (September 1996) at 11. Arbitrarily excluding these carriers from the compensation obligation has the effect of increasing the tax on the larger IXCs by 25%, while giving all other carriers the competitive advantage of a free ride.

III. BASING THE PER-CALL RATE ON THE DEREGULATED LOCAL COIN RATE AFTER THE SECOND YEAR CREATES ADMINISTRATIVE PROBLEMS AND A HUGE POTENTIAL FOR FRAUD (¶¶70-71)

The Commission has opened Pandora's Box by determining that after the second year, the amount of compensation (in the absence of the highly unlikely event of an agreement between a PSP and an IXC to pay some lower amount)[8] is whatever the PSP

[7] LECs may handle both intraLATA toll-free calls and intraLATA 0+ calls from private payphones. Moreover, GTE and SNET are now engaged in long distance service from within their regions, and many of the RBOCs have begun to offer out-of-region long distance service.

[8] The only bargaining power IXCs have in attempting to get a lower rate is the threat to block calls from a particular payphone. Such blocking is not costless to IXCs -- it

chooses to charge, on a deregulated basis, for local coin calls. This creates substantial administrative problems. First, it is unclear whether, under the Commission's order, the applicable rates for purposes of the compensation from IXCs, are those in effect at the beginning of a billing period (e.g., a calendar quarter) or at the end of the billing period, or can vary within this period. Allowing the rates to vary from one phone to the next, in and of itself, adds substantially to the processing resources required to track and pay the compensation; having the rate from a particular payphone change during a billing period creates even greater administrative complexities. It would not simply be enough to run one quarter's worth of data against a rate table; instead, the data would have to be run, day by day, against rate tables that could vary from one day to the next.

The Commission's ill-advised scheme also creates a very real problem of verification: in dealing with an industry, some members of which have spawned the problem of price gouging, are IXCs expected to accept, at face value, whatever amount the PSPs claim their local rate is? The only alternative would be for the IXCs to send out "phone police"

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consumes additional switching resources and requires programmer time to update the translation tables. More importantly, it is far from clear whether IXCs could exercise that threat and at the same time remain viable competitors in the provision of travel services to the public or toll free service to commercial customers, since all such customers desire universal service coverage.

to verify the local rates charged from each of the 1.85 million payphones in the U.S., an administrative expense that would either have to be deducted from the compensation amounts due to PSPs or passed on to consumers in the form of higher rates. In the absence of an effective mechanism to verify the local coin rates charged at various payphones, unscrupulous PSPs can be expected to claim inflated rates. And if that compensation were not enough to satisfy the PSP, it could send one of its employees around to each of its phones periodically and dial several subscriber 800 numbers in order to ensure that the phone generates substantial compensation. At the $.35 rate prescribed for the second year, a PSP could generate $84 an hour of revenue on each phone by paying someone to dial toll free subscriber numbers.[9] Even paying someone $10 an hour to dial toll free numbers would yield a net profit to the PSP of $74 per hour. If the PSP instead were to charge $1.00 for a local coin call, it could generate gross revenues of $240 an hour through such a means. Sprint is unaware of any existing IXC capability to detect such fraud.[10]

Even assuming good faith on the part of all PSPs, a PSP believing that the price elasticity of local coin calls is low

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[9] This assumes connecting to four toll free numbers per minute, which is well within the capability of any person of average manual dexterity.

[10] Such calls would be spread out among a number of different service providers and might never trigger fraud alarms for any one carrier.

may choose to charge a high local calling rate in the deregulated environment the Commission has created and thereby inflate its compensation from interexchange calls placed on the phone as well.[11]

IV. INTERNATIONAL CALLS SHOULD NOT BE INCLUDED AS COMPENSABLE CALLS (¶54)

In the NPRM, the Commission relied on §§4(i) and 201(b) as providing authority for treating international calls as compensable, even though §276 limits any such program to "intrastate and intestate" calls. In its Comments (at 8), Sprint pointed out that §4(i) limits Commission actions to those not inconsistent with the Act and argued that §201(b) has no apparent relevance to the issue at hand. Sprint also argued (id.) that there was no basis for the Commission's assumption that Congress intended to include international calls when the terms it used did not include such calls in a statute that is otherwise replete with references to international and foreign communications. Notwithstanding these arguments and similar arguments of other parties (see e.g., MCI Comments at 4), the Commission continues to rely on §§4(i) and 201(b) -- still without explaining the relevance of these provisions -- and to infer a Congressional intent,

[11] Even if the PSP believed the demand for local coin calls is relatively high, the PSP might be willing to trade a lower number of such calls in return for higher compensation from IXCs.

without any support in the legislative history, that goes well beyond the words Congress chose to use.

V. THE SET USE FEE METHOD SHOULD BE ADOPTED (¶¶83-84)

The Commission should reconsider its adoption of the "carrier-pays" approach to PSP compensation and instead opt for the "set use fee" method. The only reason given for not adopting the set use fee is the allegedly greater transaction costs. However, no attempt was made to estimate the magnitude of these costs. All that is involved is the up-front programming expense of adding an additional line item to the telephone bill. Moreover, while the set use fee could be regarded as non-taxable revenue for the IXC,[12] the carrier-pays method inflates the taxable gross receipts of the IXCs, and the increased taxes will ultimately have to be passed onto consumers. These added taxes could rapidly outweigh the programming expenses involved in implementing the set use fee. Finally, in the absence of having the party using a payphone pay the PSP directly for the use of the phone, the set use fee method is the most cost-causative means of assessing the payphone compensation charge, and has the virtue of giving visibility to the public of the amount of "tax" the government is imposing on them.

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[12] See Sprint's Comments at 12-13.

VI. THE REPORT AND ORDER UNFAIRLY BURDENS "FACILITIES-BASED CARRIERS" WITH THE OBLIGATION TO COMPENSATE PSPs ON BEHALF OF RESELLERS (¶86)

In ¶86, the Commission concluded that "in the interests of administrative efficiency and lower costs, facilities-based carriers should pay the per-call compensation for the calls received by their reseller customers." (Footnote omitted.) Apart from the fact that the Commission fails to define either the term "facilities-based carriers" or "reseller,"[13] it is unfair to require "facilities-based carriers," however defined, to shoulder the per-call compensation obligations for the resellers that use their facilities. It may be more administratively efficient and less costly for resellers to be relieved of this obligation, but the same is not true of the facilities-based carriers to whom this obligation is shifted.

In the first place, the Commission provides no guarantee that the facilities-based carriers will recover the compensation occasioned by calls handled by resellers from those resale carriers. Although the Commission expresses the belief in ¶86 that IXCs could "negotiat[e] future contract provisions" that would make them whole, there is no record support that the facilities-based IXCs would be able to do so. Some of Sprint's contracts with resale carriers may be

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[13] As far as Sprint is aware, all IXCs -- including Sprint, AT&T and MCI -- resell, to some degree or other, the services and/or transmission facilities of other carriers.

interpreted as precluding Sprint from passing through these charges for the term of the contract. And once those contracts expire, Sprint would have no leverage to be made whole for the past payphone charges it has absorbed; if it tried to do so through rates for future service, the resellers could shift their business to a different facilities-based carrier.

Furthermore, even if the facilities-based carriers were contractually able to pass the per-call compensation through to their reseller customers, it is likely that they would be caught in the middle of disputes between resellers and PSPs as to how much the reseller owes. The facilities-based carrier may have no way of knowing whether a call handled by a reseller is a "completed" call[14] and thus has no way of ascertaining how much is owed to PSPs from particular resellers.

Under the Commission's resale policy, facilities-based carriers have no choice but to resell their services to competing carriers. There is no reason to force facilities-based carriers to shoulder the compensation obligations that are properly attributable to their reseller-competitors, particularly in the absence of any assurance that the facilities-based carriers can fully pass on to their resellers

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[14] This is particularly true in the case of operator service and prepaid card calls.

the amounts attributable to the calls handled by the resellers, and the administrative expense related thereto.[15] The Commission found, in ¶97, that the carrier that is the primary economic beneficiary of a payphone call should be responsible for tracking the call. Clearly, the reseller is the primary beneficiary. If, as the Commission believes (id.), it is feasible for the larger facilities-based IXCs to contract out their call tracking and compensation functions in order to ease the administrative burdens on them, then there is no reason why the Commission should not expect smaller IXCs to be able to do so as well. Thus, PSPs should be responsible for billing all IXCs from whom they expect payment, and no IXC should be required to track calls or pay compensation to PSPs on behalf of any other carrier, unless that IXC has contractually agreed to do so on behalf of the other carrier.[16]

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[15] The Commission offers no statutory authority for the proposition that it can force facilities-based IXCs to perform these functions.

[16] The relevant rules -- "deferred" §§64.1300(a) and 64.1310(a) -- place the compensation and tracking obligations on "each" or "every" "carrier to whom [a call] is routed." Read literally, these provisions could require compensation to be paid several times for each call, since the call is routed to a LEC on each end of the call, and through one or more IXCs. Instead, the rules should place the compensation and tracking obligations on the carrier that charges the end user for the call.

VII. TRANSMISSION OF INFO DIGITS MUST BE AN EXPLICIT CONDITION FOR ELIGIBILITY (¶98)

Although in ¶98 of the Report and Order, the Commission agreed with Sprint and MCI that each payphone should be required to generate 07 or 27 coding digits within the ANI to enable carriers to track calls, §64.1310 of the Rules does not reflect this requirement. Instead it requires compensation to be paid to phones that appear on a LEC-generated list of payphones, or phones for which the PSP provides alternative verification, as spelled out in paragraph (e) of that section. Thus, it is possible that a PSP could claim compensation for calls made via its phones pursuant to §64.1310 even though those phones do not generate the info digits IXCs need for tracking. Accordingly, §64.1310 should be amended to track the order by making the transmission of the info digits from the payphone an explicit condition of eligibility for compensation.

VIII. LECs MUST BE REQUIRED TO PROVIDE, FREE OF CHARGE, A COMPREHENSIVE LIST OF EMERGENCY NUMBERS (§64.1300)

Section 64.1300(b) exempts emergency numbers from the compensation obligation. In some instances, emergency calls may be toll calls that are handled by an IXC. In order for IXCs to ensure that they are not paying compensation for emergency calls (or passing such compensation on to the calling party) they need a comprehensive and continually updated list of emergency numbers from the LECs. Because the

LECs are the primary beneficiaries of this compensation plan, they should provide this information without charge to the IXCs.

IX. ALL PAYPHONE-RELATED COSTS, NOT JUST THE COST OF THE PAYPHONE ITSELF, MUST BE REMOVED FROM CARRIER COMMON LINE CHARGES (¶183)

Paragraph 183, which directs LECs to file tariffs removing payphone costs from the carrier common line charge, does not spell out in detail all of the costs that must be removed. It is possible that a LEC might construe that paragraph as allowing it merely to reduce its CCLC by the amount of the payphone equipment costs that are transferred from the regulated to non-regulated books. The payphone costs now recovered through the CCL include far more than cost recovery for the phone itself: the local network used for payphone services, and local business office expenses. In order to carry out Congress' mandate in §276(b)(i)(B) that all payphone subsidies be removed from exchange and exchange access revenues, the Commission should clarify the LECs' obligations to that effect.

X. THE COMMISSION CANNOT REQUIRE LECS TO PROVIDE MAINTENANCE AND INSTALLATION SERVICES (¶149)

Paragraph 149 of the Report and Order requires LECs to provide, among other things, "installation and maintenance of basic payphone services...to other providers of payphone services on a non-discriminatory basis." Sprint assumes that the reference to installation and maintenance refers to the phone lines used to connect a payphone to the LEC's network, rather than installation and maintenance of the payphone itself. The latter activities, with the change in treatment of LEC provided payphones to non-regulated equipment, do not constitute telecommunications services, and it is not self-evident that the Commission has any jurisdiction to require LECs to provide such services to their competitors. Thus, the Commission should clarify that the required "service" offerings relate only to payphone lines, not the payphones themselves.

XI. CONCLUSION

The Commission's payphone compensation program is misconceived in every important respect. Sprint urges the Commission to rescind its Report and Order in toto.

Respectfully submitted,

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CERTIFICATE OF SERVICE

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